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SUBJECT: Polish consumer e-commerce: Considerations for new entrants.

REF: A) Warsaw 00735, B) Warsaw 01117

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Summary

¶1. Leading Polish internet players have a recipe for success in the Polish and other central European internet markets. New entrants following the lead of these players should consider online infrastructure, logistics, consumer market characteristics and online consumer behavior when making the decision to invest. End Summary.

Who Are the Market Leaders?

¶2. As mentioned in ref A, the Polish online consumer market is expected to grow to 16 billion zloty ($5.4 billion) by 2010. Stepping up to serve Polish online consumers are internet auction houses and regular online stores. The most successful auction house is Allegro.pl, with 2.5 billion ($950,000) zloty in sales for 2006, 7 million monthly users, and almost 2 million active auctions at any time. With one eighth the active auctions, rival Swistak comes in at second place, followed closely by ebay.pl. Among online stores, Merlin leads with a little more than 60 million Zloty ($19 million) in sales and 1.65 million monthly users, followed by wysylkowa.pl and empik.com. American giant Amazon.com comes in fourth with 615,000 monthly users.

What Are their Recipes for Success?

¶3. The recipe for success of Allegro, Merlin, and other Polish internet players includes being the first to market and having an understanding of the Polish marketplace. These factors perhaps explain why American giants ebay and Amazon are still far behind in monthly customer visits. Polish internet players are now using this recipe to expand into other central and eastern European markets where competitors are few and market preferences similar. Allegro already has a majority share in Hungarian and Czech markets, and instant messenger player Gadu-Gadu has successfully established a presence in the Baltic States. For many, the next target is Ukraine, which has been described as "Poland circa 2000".

¶4. It is clear that being the first major player to market is a key advantage over subsequent rivals. Both Allegro and Gadu-Gadu established a strong domestic presence before the arrival of eBay and Skype and maintain number-one positions in their respective markets.

¶5. While it may be a matter of time and additional experience before newer entrants can overcome the first-to-market advantage of the current leaders, an understanding of the Polish market is also important to success. Specifically, what challenges and market peculiarities should new entrants be aware of. Our discussions with a public relationship specialist for Merlin identified the following: online infrastructure, logistics, consumer price sensitivity, and internet behavior.

What are the Challenges?

¶6. One major challenge is the volume of Polish business interactions that are still conducted on paper, which means that new entrants may face supply chains that are not yet "internet ready" when setting up their businesses. In Merlin's case, there was no comprehensive electronic registry of Polish publications, a critical component for an online bookstore. In the end, Merlin created its own registry - an intensive and painstaking process. There has been one advantage - Merlin created a competitive advantage for itself and is now able to sell access rights to its publications database to other interested partiesinthe Polish publishing industry.

¶7. Another challenge is fulfilling customer orders. The lower volume of orders and relatively poorer transport infrastructure in Poland made timely, cost effective deliveries to rural areas difficult. Merlin experienced standard delivery times of three to four weeks, and damaged deliveries are a consistent problem. Package tracking availability and reliability is inconsistent. Although such delivery services are technically outside of Merlin's control, they are an important consideration and will become more so

as Polish consumer demands for delivery reliability and information mature.

Consumer Behavior

¶8. Besides some challenges associated with setting up an online business, Polish online consumer characteristics are important to product mix, website design, and payment type. Merlin's continued focus on lowest price offerings indicates that even with the growth and diversification of the Polish consumer market, the Polish consumer continues to be price sensitive. As mentioned in ref B, this sensitivity to price is reflected by the popularity of price comparison websites such as ceneo.pl, and by the relatively low market share of more expensive "lifestyle" products such as apple's iPod, which comprises only 3% of the Polish mp3 player market.

¶9. Additionally, the Polish online consumer spends more time per online session than others, and is not yet comfortable with finding online solutions to questions - an overwhelming majority of consumers still prefer to call the helpdesk. Only 2% of Merlin customers use online tools to determine the status of their order. This suggests that user-friendly websites can generate additional purchases while reducing customer support expenses.

¶10. Another interesting characteristic is that Polish online consumers avoid credit card payments. Cash on delivery and electronic funds transfers each account for 35% of purchases; pre-payments into Merlin customer accounts at the post office, a further 5%. Credit cards account for only 25%, making other payment methods vital to the success of any new entrant in the Polish marketplace.

Comment

¶11. The Polish internet market, while potentially lucrative, still encounters infrastructure and logistical challenges. In addition, Polish consumers' online behavior and payment preferences suggest that while the average online user can browse the internet, there is a lower level of expertise and comfort when it comes to locating, ordering, requesting help, and paying for products and services online. Despite this, Polish market leaders have been successful in Poland and are using their experience to expand into surrounding countries.

¶12. In order to maximize the chance of success, there are two strategies new entrants to the Polish market may wish to consider. One strategy is partnering with a local firm that can help new entrants understand the local market, its peculiarities, set up considerations, and any supply chain and infrastructure challenges. A second strategy is focusing on a product or service that is appropriate for the current level of online market development, delivery capability, and online consumer price sensitivity, behavior, and maturity.

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